

## Part III

### Administrative, Procedural, and Miscellaneous

26 CFR 601.601: Rules and regulations.  
(Also Part I, § 163)

Rev. Proc. 2008-51

#### SECTION 1. PURPOSE

This revenue procedure describes circumstances in which the Internal Revenue Service (“Service”) will not treat a debt instrument as an applicable high yield discount obligation (“AHYDO”) for purposes of §§ 163(e)(5) and 163(i) of the Internal Revenue Code.

This revenue procedure provides certainty with respect to certain potential tax issues that may be implicated by the issuance of a debt instrument (including a deemed issuance of a debt instrument under § 1.1001-3 of the Income Tax Regulations) in the circumstances described below. No inference should be drawn about whether similar consequences would obtain if a debt instrument falls outside the limited scope of this

revenue procedure. Furthermore, there should be no inference that, in the absence of this revenue procedure, a debt instrument within its scope would be an AHYDO.

## SECTION 2. BACKGROUND

.01 Corporations frequently obtain financing commitments (“Financing Commitments”) from potential lenders (“Lenders”) in advance of borrowing money. These Financing Commitments ensure that the corporation will have sufficient debt financing at a future date, within certain parameters (for example, the total amount to be borrowed, an interest rate not to exceed a certain level, and the term of the loan).

.02 In some cases, the Financing Commitments are not ultimately called upon by the corporation, and the corporation obtains debt financing from other sources (or doesn’t borrow at all).

.03 In other cases, the Financing Commitments are called upon by the corporation, and the Lender extends credit pursuant to terms negotiated earlier, as part of the Financing Commitment. In some of these situations, the corporation will borrow on terms that were generally established in the Financing Commitment, and which generally remain fixed (or “permanent”) over the term of the resulting debt instrument. (The “permanent” nature of the terms frequently allows the debt to be quickly sold by the Lender to other holders.) Alternatively, the corporation will borrow on terms that are temporary (for example, in effect for a year or less) but that change to different, more “permanent” terms (that is, terms that will last for the remaining term of the financing arrangement) after this temporary period. (The corporation may attempt to refinance the loan during the temporary, or “bridge,” period on terms that are more favorable than

the “permanent” terms embedded in the loan extended pursuant to the Financing Commitment.)

.04 As recent events have demonstrated, market conditions can worsen, in an unanticipated fashion, between the time a binding Financing Commitment is obtained by the corporation and the time the corporation calls upon the Lender to perform pursuant to the Financing Commitment. This can have a number of collateral economic consequences, which can potentially result in situations in which the issue price of a debt instrument is significantly less than the amount of money actually received by the corporation, viewing the transactions as a whole. For example:

(1) In situations in which a corporation issues debt with “permanent” terms previously established in the Financing Commitment (that is, debt without temporary, or “bridge,” terms), the Lender may be unable to sell the debt to third parties for a price equal to (or near) the amount of money provided to the corporation pursuant to the Financing Commitment. In these situations, the issue price of the debt may be significantly less than the amount of money advanced to the corporation. For example, this result could occur, in certain circumstances, if the Lender sells a substantial amount of the debt to third parties in its capacity as an underwriter within the meaning of § 1.1273-2(e).

(2) In situations in which a corporation issues debt with temporary, or “bridge,” terms previously established in the Financing Commitment, the corporation may be unable to refinance the debt in the capital markets with new, alternative, “permanent” debt financing with terms that are more (or equally) favorable than the

“permanent” terms embedded in the debt issued pursuant to the Financing Commitment. Thus, in order to allow the Lender to sell the debt to third parties (whether as part of a separately negotiated transaction or because the corporation is required to do so by contract), the parties may amend the terms of the debt to make it more marketable. Depending on the facts of a given case, such amendments may constitute a “significant modification” within the meaning of § 1.1001-3. In this situation, the issue price of the new debt, deemed to have been issued to retire the old debt, may be significantly less than the amount of money initially advanced to the corporation. For example, this result could occur, in certain circumstances, if the new debt is traded on an established market within the meaning of § 1.1273-2(f).

.05 The issuance of a debt instrument pursuant to a Financing Commitment (or pursuant to the significant modification of a debt instrument originally issued pursuant to a Financing Commitment) potentially raises adverse income tax consequences in situations in which the issue price of the debt instrument is less than the cash actually received by the corporation for the debt instrument issued pursuant to the Financing Commitment. For example, interest deductions on the debt instrument may be disallowed under § 163(e)(5).

### SECTION 3. APPLICABLE LAW

.01 Under § 163(e)(5), in the case of an AHYDO, a corporation is not allowed a deduction for the disqualified portion of the original issue discount (“OID”) on the obligation, and the corporation’s deduction for the remaining portion of the OID is

deferred until the OID is paid in cash or in property (other than debt of the issuer or a related person within the meaning of § 453(f)(1)).

.02 Section 163(i) defines an AHYDO as any debt instrument if:

(1) The maturity date of the debt instrument is more than five years from the date of issue;

(2) The yield to maturity of the debt instrument equals or exceeds the sum of the applicable Federal rate in effect under § 1274(d) for the calendar month in which the instrument is issued plus five percentage points; and

(3) The debt instrument has significant OID.

.03 Under § 163(i)(2), a debt instrument has significant OID if:

(1) The aggregate amount that would be includible in gross income with respect to the debt instrument for periods before the close of any accrual period (as defined in § 1275(a)(5)) ending after the date five years after the date of issue, exceeds

(2) The sum of the aggregate amount of interest to be paid under the debt instrument before the close of the accrual period, and the product of the issue price of the debt instrument (as defined in §§ 1273(b) and 1274(a)) and its yield to maturity.

.04 For purposes of determining whether a debt instrument is an AHYDO, § 163(i)(3) provides that any payment under the debt instrument is assumed to be made on the last day permitted under the debt instrument, and any payment to be made in the form of another debt instrument of the issuer (or a related person within the meaning of § 453(f)(1)) is assumed to be made when such debt instrument is required to be paid in cash or in property other than such debt instrument.

.05 Section 1.1001-3 provides rules to determine whether a modification of the terms of a debt instrument results in an exchange of the original debt instrument for a modified instrument that differs materially either in kind or in extent. Section 1.1001-3 applies to any modification of a debt instrument, regardless of the form of the modification (including an exchange of a new debt instrument for an existing debt instrument).

#### SECTION 4. SCOPE

This revenue procedure applies to a debt instrument described in either section 4.01, section 4.02, or section 4.03 of this revenue procedure.

##### .01 Debt Instrument Issued For Money Pursuant to a Financing Commitment.

The debt instrument is issued by a corporation and--

(1) The debt instrument is issued for money and the terms of the debt instrument are consistent with the general terms of a binding Financing Commitment obtained by the corporation from an unrelated party before January 1, 2009; and

(2) The debt instrument would not be an AHYDO within the meaning of § 163(i), if, solely for purposes of making a determination under this section 4.01(2), the issue price of the debt instrument were the net cash proceeds actually received by the corporation for the debt instrument (regardless of whether a different issue price is determined under § 1.1273-2).

.02 Debt Instrument Exchanged for a Debt Instrument Issued Pursuant to a Financing Commitment. The debt instrument is issued by a corporation and--

(1) The debt instrument is issued in exchange (including a deemed exchange under § 1.1001-3) for a debt instrument (“Old Debt Instrument A”) issued by the corporation and described in section 4.01 of this revenue procedure;

(2) The debt instrument is issued within 15 months following the issuance of Old Debt Instrument A;

(3) The debt instrument would not be an AHYDO within the meaning of § 163(i), if, solely for purposes of making a determination under this section 4.02(3), the issue price of the debt instrument were the net cash proceeds actually received by the corporation for Old Debt Instrument A (regardless of whether a different issue price is determined under § 1.1273-2 or § 1.1274-2, whichever is applicable);

(4) The maturity date of the debt instrument is not more than one year later than the maturity date of Old Debt Instrument A; and

(5) The stated redemption price at maturity of the debt instrument is not greater than the stated redemption price at maturity of Old Debt Instrument A (see § 1.1273-1(b) to determine the stated redemption price at maturity of a debt instrument).

.03 Debt Instrument Indirectly Exchanged for a Debt Instrument Issued Pursuant to a Financing Commitment. The debt instrument is issued by a corporation and--

(1) The debt instrument is issued in exchange (including a deemed exchange under § 1.1001-3) for a debt instrument (“Old Debt Instrument B”) issued by the corporation and described in section 4.02 of this revenue procedure;

(2) The debt instrument is issued within 15 months following the issuance of Old Debt Instrument A;

(3) The debt instrument would not be an AHYDO within the meaning of § 163(i), if, solely for purposes of making a determination under this section 4.03(3), the issue price of the debt instrument were the net cash proceeds actually received by the corporation for Old Debt Instrument A (regardless of whether a different issue price is determined under § 1.1273-2 or § 1.1274-2, whichever is applicable);

(4) The maturity date of the debt instrument is not more than one year later than the maturity date of Old Debt Instrument A; and

(5) The stated redemption price at maturity of the debt instrument is not greater than the stated redemption price at maturity of Old Debt Instrument A (see § 1.1273-1(b) to determine the stated redemption price at maturity of a debt instrument).

#### SECTION 5. APPLICATION

If this revenue procedure applies to a debt instrument, the Service will not treat the debt instrument as an AHYDO for purposes of §§ 163(e)(5) and 163(i).

#### SECTION 6. EFFECTIVE DATE

This revenue procedure is effective on August 8, 2008. Sections 4.02(4), 4.02(5), 4.03(4) and 4.03(5) of this revenue procedure do not apply to debt instruments issued before August 8, 2008.

#### SECTION 7. REQUEST FOR COMMENTS

The Service invites public comment related to this revenue procedure. Comments should be submitted no later than November 15, 2008, to the Internal Revenue Service, CC:PA:LPD:RU (Rev. Proc. 2008-51), room 5203, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Comments also may be hand delivered



between the hours of 8 a.m. and 4 p.m. to the Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW, Washington, DC 20224, Attn: CC:PA:LPD:RU (Rev. Proc. 2008-51), room 5203. Alternatively, comments may be submitted via the Internet at [Notice.Comments@irs.counsel.treas.gov](mailto:Notice.Comments@irs.counsel.treas.gov). Include the revenue procedure number (Rev. Proc. 2008-51) in the subject line. All comments will be available for public inspection and copying in their entirety. Therefore, comments received by the IRS and Treasury should not include taxpayer-specific information or of a confidential nature. Comments should include the name and telephone number of a person to contact.

#### SECTION 8. DRAFTING INFORMATION

The principal author of this revenue procedure is William E. Blanchard of the Office of Associate Chief Counsel (Financial Institutions and Products). For further information, contact Mr. Blanchard on (202) 622-3950 (not a toll-free call).